

REPORT OF EXAMINATION
OF THE

SIERRA HEALTH AND LIFE
INSURANCE COMPANY, INC.

AS OF
DECEMBER 31, 2004

Participating States
and Zones:

California
Nevada

Filed August 19, 2005

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Los Angeles, California
August 16, 2005

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable John Morrison
Secretary, Zone IV-Western
Commissioner of Insurance and Securities
Montana Department of Insurance
Helena, Montana

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman and Commissioners:

Pursuant to your instructions, an examination was made of the

SIERRA HEALTH AND LIFE INSURANCE COMPANY, INC.

(hereinafter also referred to as the Company) at its home office located at 2720 North Tenaya Way, Las Vegas, Nevada. The Company's statutory home office is located at 300 South Grand, Suite 2200, Los Angeles, California.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2001. This examination covers the period from January 1, 2002 through December 31, 2004. The examination was conducted by the California Department of Insurance pursuant to the National Association of Insurance Commissioners' (NAIC) plan of examination. An examiner from Nevada, representing Zone IV - Western of the NAIC participated in the examination.

The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and

an evaluation of the assets and a determination of liabilities as of December 31, 2004, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in-force by states; mortality experience; and sales and advertising.

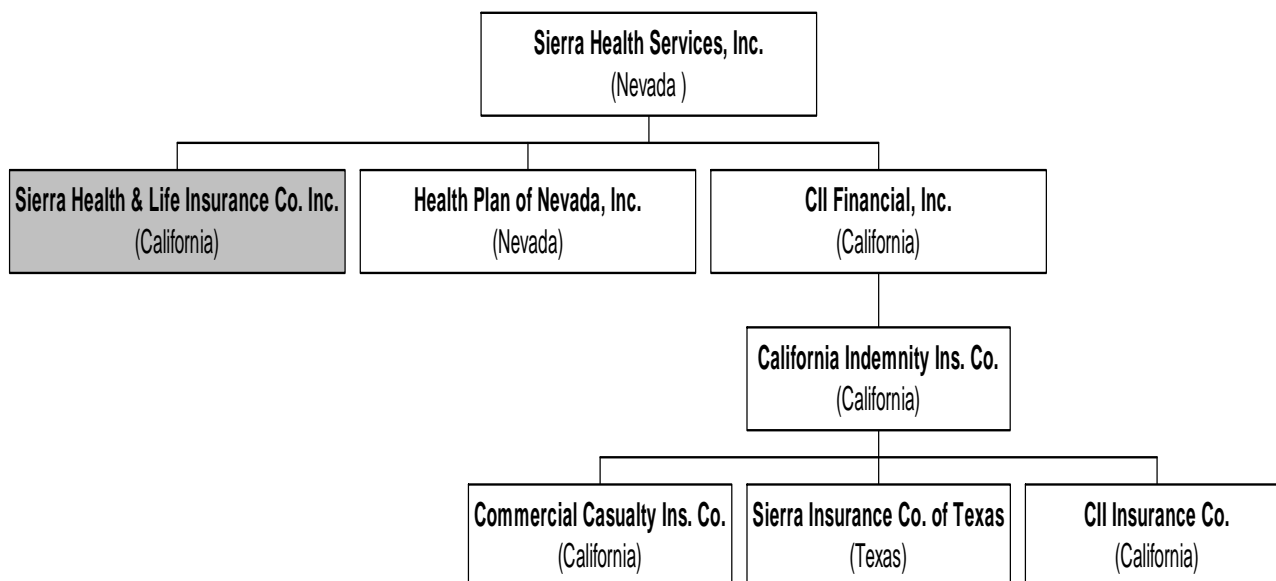
COMPANY HISTORY

The Company was formed as Sierra Health and Life Insurance Company in October 1985, and was capitalized with \$6 million in common stock and \$1 million in surplus. In June 1986, Sierra Health Services, Inc. (SHS) acquired West States Insurance Company (West States), a California domiciled health and life insurer. The Company was merged into West States, effective December 31, 1986, and was renamed Sierra Health and Life Insurance Company, Inc. In 2000, SHS contributed \$2.3 million in cash to the Company to enable it to meet the 200% of total adjusted capital pursuant to the Risk Based Capital requirements. In December 2001, SHS made an additional cash contribution to the Company in the amount of \$1 million. The Company paid a \$3 million dividend to SHS in 2004.

MANAGEMENT AND CONTROL

The Company is a wholly-owned subsidiary of Sierra Health Services, Inc. (SHS). SHS is a publicly held managed care holding company.

The following abridged organization chart, which is limited to the Company's parent along with its insurance subsidiaries, depicts the Company's relationship within the holding company system: (all ownership is 100%)



Management of the Company is vested in a nine-member board of directors. The directors and principal officers serving as of December 31, 2004 are as follows:

Directors

Name and Residence

Principal Business Affiliation

Frank E. Collins
Las Vegas, Nevada

Chairman of the Board of Directors
Sierra Health and Life Insurance Company, Inc.

Jonathon W. Bunker
Las Vegas, Nevada

President, HMO and Insurance
Sierra Health and Life Insurance Company, Inc.

Donald J. Giancursio
Las Vegas, Nevada

Vice President, Sales and Marketing
Sierra Health and Life Insurance Company, Inc.

Laurence S. Howard
Las Vegas, Nevada

Senior Vice President, Information Systems
Sierra Health Services, Inc.

Lloyd W. Isom
Las Vegas, Nevada

Owner
Insurance Management Marketing

David M. Marlon
Las Vegas, Nevada

Vice President, Business Development
Health Plan of Nevada, Inc.

Wayne R. Nippe
Las Vegas, Nevada

Secretary
Sierra Health and Life Insurance Company, Inc.

Name and ResidencePrincipal Business Affiliation

Paul H. Palmer
Las Vegas, Nevada

Treasurer
Sierra Health and Life Insurance Company, Inc.

Darren G. D. Sivertsen
Las Vegas, Nevada

Vice President, Operations
Sierra Health and Life Insurance Company, Inc.

Principal OfficersNameTitle

Jonathon W. Bunker

President

Wayne R. Nippe

Secretary

Paul H. Palmer

Treasurer

Nancy A. Lewandowski

Vice President, Assistant Treasurer and
Chief Financial Officer

Allan J. Ebbin, M.D.

Vice President, Healthcare Education

Donald J. Giancursio

Vice President, Sales and Marketing

Bonnie E. Hillegass

Vice President, Managed Care

Marlin M. Mueller

Assistant Secretary and Actuary

Michael A. Montalvo

Vice President, Customer Service Operations

Edward M. Nathan, M.D.

Vice President, Medical Management

Darren G. D. Sivertsen

Vice President, Operations

Management Agreements

On May 11, 1989, the Company entered into an Administrative Service Agreement with SHS. Under the terms of the agreement, SHS provides services such as budgeting and financial support, personnel, legal review, marketing, advertising, claims processing, development of medical management services, etc.

In compliance with the recommendation of the California Department of Insurance (CDI) during the last examination and pursuant to the California Insurance Code Sections 1215.4 and 1215.5, a new Intercompany Service Agreement (Agreement) was filed with and approved by the CDI effective January 1, 2002. Under the terms of the Agreement, reimbursement is based on charges for all services provided by SHS. The Company and SHS determine the manner and method of allocation,

on or before the end of the first quarter of any calendar year in which services are rendered. Periodically, SHS and the Company will survey the actual costs of SHS in supplying the services and the method of allocation. However, since June 2001 and for the entire examination period SHS has waived the management fees. Consequently, the Company has not paid management fees during the examination period.

TERRITORY AND PLAN OF OPERATION

The Company is a California domiciled health and life insurance company licensed in the following 43 states and the District of Columbia:

Alabama	Illinois	Montana	Rhode Island
Alaska	Indiana	Nebraska	South Carolina
Arizona	Iowa	Nevada	South Dakota
Arkansas	Kansas	New Jersey	Tennessee
California	Kentucky	New Mexico	Texas
Colorado	Louisiana	North Carolina	Utah
Connecticut	Maine	North Dakota	Virginia
Delaware	Maryland	Ohio	Washington
Georgia	Massachusetts	Oklahoma	West Virginia
Hawaii	Mississippi	Oregon	Wyoming
Idaho	Missouri	Pennsylvania	

During 2004, the Company wrote direct premiums of \$104.3 million, of which 99.2% represented accident and health business, primarily with employer group plans. The states in which the Company wrote the majority of its direct premiums were Nevada, \$78.4 million (74.6%), Texas, \$15.2 million (14.5%), Iowa, \$5.7 million (5.5%), and Louisiana, \$3.7 million (3.6%). The Company wrote approximately \$260,000 in California.

The Company's principle business is the sale of group accident and health policies to employer groups and individual Medicare supplemental policies through direct sales, brokers and general agents. Currently policies are written in California, Colorado, Iowa, Louisiana, Nevada, and Texas. The Company's core product is the Preferred Provider Organization (PPO) fully insured plan. The majority of these arrangements are with employer groups located in the State of Nevada. Prior to 2004, the Company had entered into agreements with Third Party Administrators (TPA's) for the

sales, marketing and administration of the PPO products for all business outside of the State of Nevada. In 2003, the Company terminated all of the TPA agreements for the PPO products.

In addition, the Company had an agreement with Olympic Health Management Systems (OHMS), a Washington based TPA, for marketing and administration of the Company's Medicare supplement insurance product. A new TPA based in New York, Jardine, Lloyd, Thompson Services, Inc. (JLT), was contracted beginning March 1, 2003, to administer the Medicare supplement line of business. The Medicare supplement product is currently marketed in Texas, Colorado, Iowa, Louisiana, and Nevada. In addition to the aforementioned products, the Company also sells life insurance and accidental death and dismemberment policies to employer groups and aggregate and specific stop loss policies to self insured groups.

REINSURANCE

Assumed

In 2002, the Company entered into an assumption reinsurance agreement with Health Plan of Nevada, Inc. (HPN), an affiliate, whereby the Company assumes risk for HPN's inpatient hospitalization claims in excess of \$200,000 up to \$300,000. Claims in excess of \$250,000 are reinsured by HPN under another agreement. Premiums assumed pursuant to this agreement were \$104,280, \$171,545, and \$208,940 for the years 2002, 2003 and 2004, respectively.

Starting July 1, 2004 the Company amended the assumption reinsurance agreement with HPN, whereby the Company assumes risk for HPN's inpatient hospitalization claims in excess of \$200,000 up to \$350,000. Claims in excess of \$350,000 are reinsured by HPN under another agreement.

Ceded

The following is a schedule of the ceded reinsurance contract in-force as of December 31, 2004:

Type of Contract	Reinsurer	Coverage	Reinsurer's Limits	Company's Retention
Specific Excess Reinsurance for PPO Plans	Allianz Life Insurance Company of America (ALICA)	Acute Care and Organ Transplant	\$2 million per member lifetime	\$150,000 per member annual

Other reinsurance contracts that were in effect earlier in the examination period included a specific excess reinsurance agreement for the self-funded groups and quota-share agreements for the PPO business administered by the TPA's. These agreements have all been terminated prior to December 31, 2004. A dispute under one of the quota-share agreements was settled in arbitration for \$1.3 million, during July 2004. The Company received the cash payment for this settlement in September 2004.

Reinsurance premiums ceded under all contracts were \$1,550,670, \$1,385,000 and \$985,383 for the years 2002, 2003 and 2004, respectively.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2004

Summary of Operations and Capital and Surplus Accounts
for the Year Ended December 31, 2004

Reconciliation of Capital and Surplus from
December 31, 2001 through December 31, 2004

Statement of Financial Condition
as of December 31, 2004

<u>Assets</u>	Ledger and Nonledger <u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>	<u>Notes</u>
Bonds	\$ 34,486,606	\$	\$ 34,486,606	
Stocks: Preferred	407,908		407,908	
Real estate: Property occupied by the Company	4,918,199		4,918,199	
Cash and short-term investments	27,839,381		27,839,381	
Investment income due and accrued	422,512		422,512	
Uncollected premiums and agents balances in course of collection	332,906		332,906	
Amounts recoverable from reinsurers	9,531		9,531	
Net deferred tax asset	737,544		737,544	
Electronic data processing equipment and software	512,307		512,307	
Furniture and equipment	3,087	3,087	0	
Receivables from parent, subsidiaries and affiliates	4,784,203		4,784,203	
Aggregate write-ins for other than invested assets	<u>1,081,078</u>	<u>782,943</u>	<u>298,135</u>	
Total assets	<u>\$ 75,535,262</u>	<u>\$ 786,030</u>	<u>\$ 74,749,232</u>	
<u>Liabilities, Capital and Surplus</u>				
Aggregate reserve for life contracts			\$ 82,966	(1)
Aggregate reserve for accident and health contracts			1,404,228	(1)
Contract claims: Life			83,394	(1)
Contract claims: Accident and health			23,723,831	(1)
Premiums and annuity considerations received in advance			1,742,774	
Commissions to agents due and accrued			322,219	
General expenses due or accrued			4,555,650	
Taxes, licenses and fees due or accrued			2,136,425	
Net deferred tax liability			286,209	
Amounts withheld or retained by company as agent or trustee			35,149	
Liability for benefits for employees and agents if not included above			881,303	
Miscellaneous liabilities: Asset valuation reserve			443,133	
Miscellaneous liabilities: Payable to parent, subsidiaries and affiliates			530,195	
Aggregate write-ins for liabilities			<u>132,743</u>	
Total liabilities			36,360,219	
Common capital stock		\$ 3,600,000		
Gross paid-in and contributed surplus		7,124,960		
Unassigned funds (surplus)		<u>27,664,055</u>		
Capital and surplus			<u>38,389,015</u>	
Total liabilities, capital and surplus			<u>\$ 74,749,234</u>	

Summary of Operations and Capital and Surplus Account
for the Year Ended December 31, 2004

Statement of Income

Premiums and annuity considerations	\$ 103,816,644
Net investment income	1,850,117
Amortization of interest maintenance reserve (IMR)	(25,979)
Aggregate write-ins for miscellaneous income	<u>5,696,819</u>
Total	<u>111,337,601</u>
Death benefits	282,496
Disability benefits and benefits under accident and health policies	65,684,497
Increase in aggregate reserves for life and accident and health	4,247
Commissions on premiums, annuity considerations and deposits	5,428,602
General insurance expenses	14,753,915
Insurance taxes, licenses and fees, excluding federal income taxes	2,599,410
Aggregate write-ins for deductions	<u>3,839,072</u>
Total	<u>92,592,239</u>
Net income before federal income taxes	18,745,362
Federal income taxes incurred	<u>6,018,154</u>
Net income after federal income taxes	12,727,208
Net realized capital gain	<u>188,222</u>
Net income	<u>\$ 12,915,430</u>

Capital and Surplus Account

Capital and surplus, December 31, 2003	\$ 29,143,832
Net income	\$ 12,915,430
Change in net deferred income tax	(417,419)
Change in nonadmitted assets and related items	(256,145)
Change in asset valuation reserve	3,314
Dividends to stockholders	<u>(3,000,000)</u>
Net change in capital and surplus for the year	<u>9,245,180</u>
Capital and surplus, December 31, 2004	<u>\$ 38,389,012</u>

Reconciliation of Capital and Surplus
from December 31, 2001 through December 31, 2004

Capital and surplus, December 31, 2001, per Examination			\$ 16,351,602
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$25,175,232	\$	
Change in net deferred income tax		3,161,204	
Change in nonadmitted assets and related items	3,020,984		
Change in asset valuation reserve increase	2,398		
Dividends to stockholders	<u> </u>	<u>3,000,000</u>	
Total gains and losses in surplus	<u>\$28,198,614</u>	<u>\$ 6,161,204</u>	
Net increase in capital and surplus			<u>22,037,410</u>
Capital and surplus, December 31, 2004, per Examination			<u>\$ 38,389,012</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

- (1) Aggregate Reserve for Life Contracts
- (1) Aggregate Reserve for Accident and Health Contracts
- (1) Contract Claims: Life
- (1) Contract Claims: Accident and Health

The Company was directed by the California Department of Insurance (CDI), under California Insurance Code Section 733, to retain the actuarial firm of William Mercer (WM) for the purpose of assisting this examination in the evaluation of the Company's reserves and other related phases of the examination. Based on the evaluation of the Company's reserves by actuaries from WM and the review of WM's work by a Life Actuary from the CDI, the Company's December 31, 2004 reserves have been determined to be computed in accordance with the reserving standards of the National Association of Insurance Commissioners' and accepted for this examination report.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

There are no recommendations in the current examination report.

Previous Report of Examination

Corporate Records (Page 5): It was recommended that the Company implement procedures in its board meetings to ensure compliance with California Insurance Code (CIC) Section 735. The Company complied with CIC Section 735 by submitting the prior examination to the board of directors.

Accounts and Records (Page 9): The Company should evaluate and make appropriate changes to strengthen its information system controls. The Company has complied with this recommendation and has strengthened its information system controls as well as setting up a business continuity plan.

Aggregate Reserves for Life Policies and Contracts (Page 13): It was recommended that the Company's aggregate reserves for life policies be established on the basis of an inventory of

disabled lives with an estimate for incurred but not reported disabilities. The Company complied with this recommendation.

ACKNOWLEDGEMENT

The assistance and cooperation extended by the officers and employees of the Company during the course of this examination are hereby acknowledged.

Respectfully submitted,

_____/S/_____
Samuel J. Salzman, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California

_____/S/_____
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Division of Insurance
Representing Zone IV-Western